Asset Classes for Investment

Concrete and Virtual Vehicles

for Investing in

Real and Financial Markets

A *Market Brief* ™

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Summary

In a world fraught with chaos and mischance, the smart investor takes care to build up a robust portfolio based on a multiplicity of asset classes. For this purpose, the choices include virtual products within the financial forum as well as tangible goods in the real economy.

Each type of asset sports a distinct bundle of strengths and weaknesses. For this reason, there is no such thing as a perfect vehicle for investment. In that case, a widget that's suitable for one investor might be inapt for someone else. Given the lack of a silver bullet, the adept player drums up a trenchant strategy tailored to their own profile of personal circumstances ranging from disposable income and accrued savings to asset diversification and risk tolerance.

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The assets available for investment may be classified into two broad groups: concrete and abstract. The earthy goods run the gamut from precious metals to real estate. Meanwhile the virtual products range from common stocks to government bonds. Each type of asset plays a vital role for millions of investors in the financial bazaar as well as the real economy.

The assets of the physical kind are familiar to every household. A plain example lies in hard cash in the guise of a bill or coin. Another sample is real estate in the form of a house or farm.

In a healthy economy, money is the medium of exchange for the bulk of commercial transactions. A case in point is the payment for a melon or the salary for a staffer. Not surprisingly, a wad of cash is apt to be the first way in which a thrifty person begins to build up a nest egg.

From a different angle, just about everyone likes to have a place to call their own. For this reason, the purchase of a homestead is a popular way to stockpile a heap of wealth. To begin with, a property can serve as the repository for the initial batch of capital needed to buy the abode. In addition, the value of real estate has a way of blooming with the passage of time.

Meanwhile the virtual widgets in the financial realm represent another mode of investment. The goods of this stripe come with a medley of advantages. An example lies in the ease of procuring a stock, or the spareness of effort required to hold onto the stake.

To bring up a counterexample, owning a hoard of gold bullion is wont to entail an ongoing headache. For many an investor, keeping a stockpile of modest size squirreled away in a

secure vault could well incur an annual fee amounting to a noxious percentage of the total value of the bounty.

By contrast, consider a communal pool that holds an inventory of gold. Given the scale of the operation, the stewards of the fund should be able to keep the overhead low by negotiating a wholesale rate in leasing a secure facility.

Meanwhile, at the retail end of the business, each customer could hold a clutch of shares in the communal fund with no fuss to speak of. In this setting, the main task of the investor is to conduct an ample amount of due diligence at the outset before buying into the commodity pool in the first place. After that stage, though, it's a simple matter to keep track of the shares that have been procured for a personal portfolio.

Granted, the guarded investor continues to keep tabs on the communal pool in order to note any changes that arise in its structure or operation. An example lies in an uptick in the annual fee charged by the custodians for their role in running the fund. Even so, the burden of monitoring the commodity pool along with the personal stake is sure to be much lighter than the onus of holding onto a physical cache of gold bullion.

Due to the attractions of virtual goods, a swelling throng of investors have turned to the financial arena in order to safeguard and nurture their savings. For starters, a heap of securities may be used to stockpile a mound of wealth that has already been amassed by other means such as the sale of a business by an entrepreneur. Moreover the panoply of financial gigs can serve as vehicles for growing a germinal pool of capital.

To an increasing extent, the financial tract also offers a host of ways to invest more or less directly in the real economy. As a result, a crafty player can use papery widgets to take up concrete assets as well as weightless ones.

An instance of the latter involves an asset that lies mostly or entirely within the financial sphere. A case in point is a share of stock which represents a claim on the resources of the company standing behind the equity. At a fundamental level, the arrangement is similar in the case of a bond issued by a sovereign state.

From a larger stance, a financial vehicle can also be used to venture into a tangible market. An example involves an exchange traded fund which holds a trove of silver bullion. Another sample lies in a futures contract that spells out the conditions for the purchase of crude oil at a fixed date down the line.

In these ways, a virtual vessel can provide a convenient way to gain exposure to a welter of asset classes assets and market niches. The examples in the real economy run the gamut from technology ventures and rental properties to agricultural combines and precious metals.

Given the versatility of virtual goods, many a gamer opts to focus solely on the widgets within the financial ring. A case in point is the cavalier trader who pays attention only to the data pouring out of the stock market in making a decision to buy or sell a bunch of shares. Meanwhile another punter in the futures market might focus on the conditions and events within the commodity branch to the exclusion of everything else.

If we take a step back, however, it should be clear that the real and financial markets are interlinked in gobs of ways. For this reason, a cogent view of the action in the marketplace requires a holistic approach that straddles the financial forum as well as the real economy.

Given the mass of hookups in the marketplace, the action in each domain is a cause as well as an effect of the activity in the other tract. For instance, the onset of a recession – or the mere prospect of a downturn – within the real economy may well spark a crash of the stock market. In the opposite direction, a blowup of the bourse could easily cripple the tangible economy, as showcased by the nasty recession in the U.S. following the bust of the Internet bubble around the turn of the millennium.

As these examples show, the financial bazaar is tightly bound to the physical economy. Moreover, the assets lying within each domain are also closely tied to each other. On the financial front, an example lies in the linkup between stocks and bonds. Meanwhile an instance in the real economy involves the rising cost of raw materials along with the ramp-up of the price tag for real estate ranging from existing houses to planned skyscrapers.

Given the slew of hookups between the real and financial markets, the wise investor pays heed to both domains. The need for a coherent view applies to any program of investment based on infirm goods, concrete wares, or a mixture of both.

As we saw earlier, each type of asset flaunts a distinct combo of advantages and limitations. For this reason there is no such thing as a perfect vehicle for investment. Moreover a given widget that suits one investor could well jangle someone else.

In view of the pitfalls in store, the shrewd player builds up a sensible agenda tailored to their personal circumstances. To this end, the key factors for consideration run the gamut from disposable income and accumulated savings to asset diversification and risk aversion.

Virtual Assets in Financial Markets

In line with earlier remarks, the goodies available for investment may be divided into two broad groups: concrete and abstract. The first category deals with the weighty assets to be found in the real economy, while the second cluster covers the ethereal goods in the financial patch.

The objects within each category may in turn be divided into a pair of subgroups: raw widgets and derived products. A *basic* item refers to any vehicle that gives rise to a subsequent product. An example lies in a stock that acts as the progenitor for a series of option contracts. Another sample involves a basket of currencies which serves as the fodder for a chain of futures contracts.

In this way, a *derivative* widget is an outgrowth of a primal instrument. A purely synthetic sample lies in an option contract based on a contrived index of a bunch of stock prices. The value of the artificial token will rise or fall in response to a number of factors, of which the foremost is the prevailing value of the target benchmark.

From a different angle, the goods available for investment may be classified by the type of issuer in the marketplace. On one hand, a security could be concocted by an institution

within the physical economy. A case in point is a stock option stamped out by a private company then handed out to its employees.

On the other hand, a widget could also be fielded by an outfit in the financial forum. A case in point is a futures contract, spawned by a commodity exchange, which deals with the purchase of a volume of natural gas.

There are still other ways to classify the plethora of products in the marketplace. For instance, a given instrument could give birth to a multiplicity of spinoffs – whether zero, one, or more. An example of the latter is a hard currency that serves as the underlying asset for a futures contract as well as an exchange traded fund.

Shades of Concreteness

As we have seen, one way to classify the universe of assets lies in the degree of abstraction. At one end of the scale lies tangible items such as ingots of silver or plots of land. Meanwhile the opposite end of the range harbors ethereal goods like options on a stock index, or futures contracts on an interest rate.

The two forms of assets – whether concrete or not – are handy breakdowns for the sake of discussion and analysis. Upon closer inspection, though, the classification of tokens turns out to be fuzzy rather than clear-cut. Put another way, the pair of groupings represent the end points along a continuum of abstraction.

To bring up an example, we turn once more to the currency market. In this precinct, each interaction involves an accord to buy or sell a batch of foreign exchange. For the two parties to a transaction, the value of the deal at any point is determined mostly by the prevailing rate of exchange in converting one currency into another. In other words, the conversion rate is the main factor in fixing the payoff for each actor – along with any secondary facets such as commissions to a broker.

Within the currency market, some of the transactions occur in the real economy through the purchase and sale of hard cash in the garb of bills and coins. A case in point is the exchange of one currency for another at a retail bank or a tourist office.

In the modern economy, however, the currency market resides largely in cyberspace. That is, the bulk of the trading takes place on digital platforms employed by myriads of actors ranging from commercial firms and financial institutions to private speculators and public agencies. The combined volume of currency trading throughout the planet comes out to trillions of dollars a day.

As a rule, a currency is apt to display both earthly and ethereal properties. As we noted earlier, the corporeal aspect shows up in a wad of cash as in the case of coins and banknotes.

On the other hand, the bulk of money takes abstract form. To begin with, a spew of mint is conjured out of thin air on a regular basis by a coterie of central banks round the world. The gassy money is then pumped into the financial system and the real economy by means of digital pipes on electronic networks. The bulk of the moolah is then stashed away in gauzy form by way of virtual entries on digital ledgers and ghostly records in data warehouses.

In short, money is partly a concrete object but mostly a vapory abstraction. Moreover the bulk of the trading in the currency market is a virtual activity taking place in cyberspace.

Given this backdrop, even the money used to buy and sell a product of any kind happens to be a hybrid medium that displays multiplex traits. That’s the case whether the item for sale is a palpable object, a vaporous widget, or a mixup of both.

More generally, there is no sharp boundary between the realms of the physical and virtual in the modern culture. The blurry state of affairs applies in spades to a host of assets, be they basic goods or spinoff wares.

Mashup of Asset Classes

As we noted above, the savvy player examines a variety of asset classes in order to fix up a wholesome portfolio. For this purpose, the candidate widgets include primal goods such as stocks and currencies as well as derived rigs as in options and futures.

In the larger scheme of things, the vehicles for investment can reach beyond the bounds of the financial tract. In that case, the adroit player can take up virtual widgets to invest in sundry types of assets ranging from precious metals to real estate.

At first sight, the realms of the concrete and abstract may seem like disjoint turfs. Upon closer inspection, though, the two spheres overlap in lots of ways.

The mashup of the physical and virtual applies to singular assets as well as their mutual interactions. A case in point is the impact of the financial bazaar on the course of the real economy.

In line with an earlier example, the burst of a bubble in the stock market can obliterate trillions of dollars at a stroke. The thumping crush of wealth on the bourse prompts millions of private investors as well as commercial firms to rein in their expenditures across the board. The clampdown on spending knocks the wind out of the entire economy and shoves it into a tailspin.

In the converse direction, the stock market tends to act as a bellwether for the economy at large. For this reason, a slump in economic output – whether actual or prospective – can pummel the bourse, ofttimes around half a year in advance.

To bring up an example of the tie-ups at work, consider the tidal wave of secular growth in the emerging regions of the world. One consequence is a lusty demand for raw materials in tandem with an uptrend in the cost of input factors for producers of all stripes. The commodities swept aloft by the groundswell run the gamut from iron and copper to oil and rubber.

The upsurge of demand prods the producers into expanding their operations by tapping into fields of lower quality. The resulting increase in the cost of extraction has to be passed onto their customers at the wholesale level. The inevitable outcome is a crank-up of prices for intermediate goods as well as finished products.

In order to tone down the flare-up of inflation, the central bank takes steps to shrink the pool of money sloshing around the financial system. The squeeze on the money supply duly pumps up the cost of capital, thus shrinking the flow of funds into the upgrade of existing facilities as well as the launch of brand-new ventures.

In addition, the hike in the cost of credit crimps the zeal for spending by the mass of consumers. The upshot is a double whammy of shrinking sales and bulging costs for vendors of all breeds.

The quandary is similar in the public sector. A showcase lies in the shriveling of income taxes and other receipts at all levels of administration ranging from the municipal agency to the national government.

As a rule, the prospect of shrunken earnings in the future tends to clobber the stock market roughly half a year in advance. The whomp of the bourse slashes the amount of wealth tucked away in the portfolios of individual investors as well as corporate treasuries.

The mass rubout of wealth acts as an additional choke on the pulse of economic activity. In these and other ways, the real and financial markets affect each other in a convoluted fashion on a continual basis.

Making Headway in Stormy Markets

Given the endless hail of upthrows in the marketplace, the sage investor takes pains to construct a hardy portfolio that contains a variety of asset classes. To this end, the choices at hand include virtual goods in the financial theater as well as tangible plums in the real economy.

To compound the challenge of investment, the financial sphere affects – and is affected by – the goings-on in the physical economy. The scrambling of the markets rattles the panoply of assets ranging from basic securities and derived rigs to raw materials and real estate.

On a positive note, though, the canny investor can turn to the financial tract as a way to invest in abstract assets as well as concrete ones. An example of the latter involves an exchange traded fund focused on the housing sector, whose fortunes rise and fall mainly in line with the outlook for the property market.

Another exemplar is a communal fund that holds a storehouse of gold bullion. In the short run, the price of the yellow metal – and thus the value of any stake held by an investor – is determined largely by the gamers plying their trade within the confines of the futures market. Even so, the outcome over the long range is slated to result mostly from the matchup of supply and demand in the global economy at large.

As these examples show, the financial forum offers the nimble player a host of choices for thrashing out a sturdy program of investment. For this purpose, the tools on hand include primal assets such as stocks and currencies as well as derivative goods as in options and futures.

Each type of widget displays a unique blend of drawcards and drawbacks. In that case, the bad news for a slouch in search of pat answers is that there's no such thing as a cure-all that befits everyone.

From a different pose, a widget that attracts one player could easily repel the next person. Hence the lack of a panacea.

To add to the muddle, the marketplace does not stand still as time goes by. For one thing, the assets in the real and financial marts have a custom of bouncing around over the short term rather than pressing ahead in a steady fashion.

Furthermore, the financial bazaar has a way of evolving over the long range; and likewise for the real economy. An example involves a communal fund that blows up or fizzles out

then fades into the night. Another sample is a brand-new instrument that expands the palette of tools available to an investor bent on drawing up a multihued portfolio. A third sample involves the demise of a fusty industry or the upgrowth of a novel lifestyle.

Meanwhile the story is similar at level of the lone investor. That is, the needs and wants of each actor are wont to change over time even in the absence of any upheavals in the external environment.

On the bright side, though, the real and financial markets offer a diversity of asset classes for drumming up a staunch portfolio. To this end, the artful investor has to design a sound strategy tailored to their own lineup of personal factors ranging from income streams and retirement plans to asset diversification and risk tolerance.